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Southeast Minnesota Economic and Business Conditions Report Fourth Quarter 2018

King Banaian
St. Cloud State University, kbanaian@stcloudstate.edu

Richard MacDonald
St. Cloud State University, macdonald@stcloudstate.edu

Southeast Minnesota
Economic and Business Conditions Report
Fourth Quarter 2018

This issue is part of a series for the six planning areas of Minnesota –
Central, Northeast, Northwest, Southeast, Southwest, and Twin Cities.
The Southeast Minnesota Planning Area consists of 11 counties:
Dodge, Fillmore, Freeborn, Goodhue, Houston, Mower, Olmsted, Rice, Steele, Wabasha, and Winona.

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EXECUTIVE SUMMARY

A slowing of economic growth over the next several months is expected in the Southeast Minnesota planning area according to the prediction of the Southeast Minnesota Index of Leading Economic Indicators (LEI). The leading index fell by 9.81 points in the fourth quarter as all five index components recorded negative values. A decrease in the number of Rochester area residential building permits, a weakening in consumer sentiment, lower new filings of incorporation and LLC, and a decline in the Minnesota Business Conditions Index all helped drive the LEI lower in the fourth quarter. The LEI is now essentially unchanged from one year ago.

There were 804 new business filings with the Office of the Minnesota Secretary of State in Southeast Minnesota in the fourth quarter of 2018 — representing a 4.7 percent reduction from one year ago. 70 new regional business incorporations were filed in the fourth quarter, 48.9 percent more filings than prior year levels. At a level of 498, fourth quarter new limited liability company (LLC) filings in Southeast Minnesota were 5.7 percent lower than in the fourth quarter of 2017. With 182 filings, new assumed name activity was 20.2 percent below what was seen in the same quarter last year. There were thirteen more new filings for Southeast Minnesota non-profit over the last three months compared to one year earlier.

Sixty-one percent of new business filers in the Southeast Minnesota planning area completed the voluntary Minnesota Business Snapshot (MBS) survey in the fourth quarter. Results of this voluntary survey indicate that 7.3 percent of new filers come from communities of color and 6.7 percent are veterans. Only 2 percent of new filers come from the disability community and 4.5 percent of new filings are made by the immigrant community. Nearly forty-one percent of new business filings in Southeast Minnesota in the fourth quarter were initiated by women. MBS results also show that most new business filers in Southeast Minnesota have between 0 and $10,000 in annual gross revenues (although 47 new filers have revenues in excess of $50,000). The most popular industries for new businesses in Southeast Minnesota are retail trade, real estate/rental/leasing, construction and other services. Employment levels at most new firms are between 0 and 5 workers, and 47.6 percent of those starting a new business consider this a part-time activity.

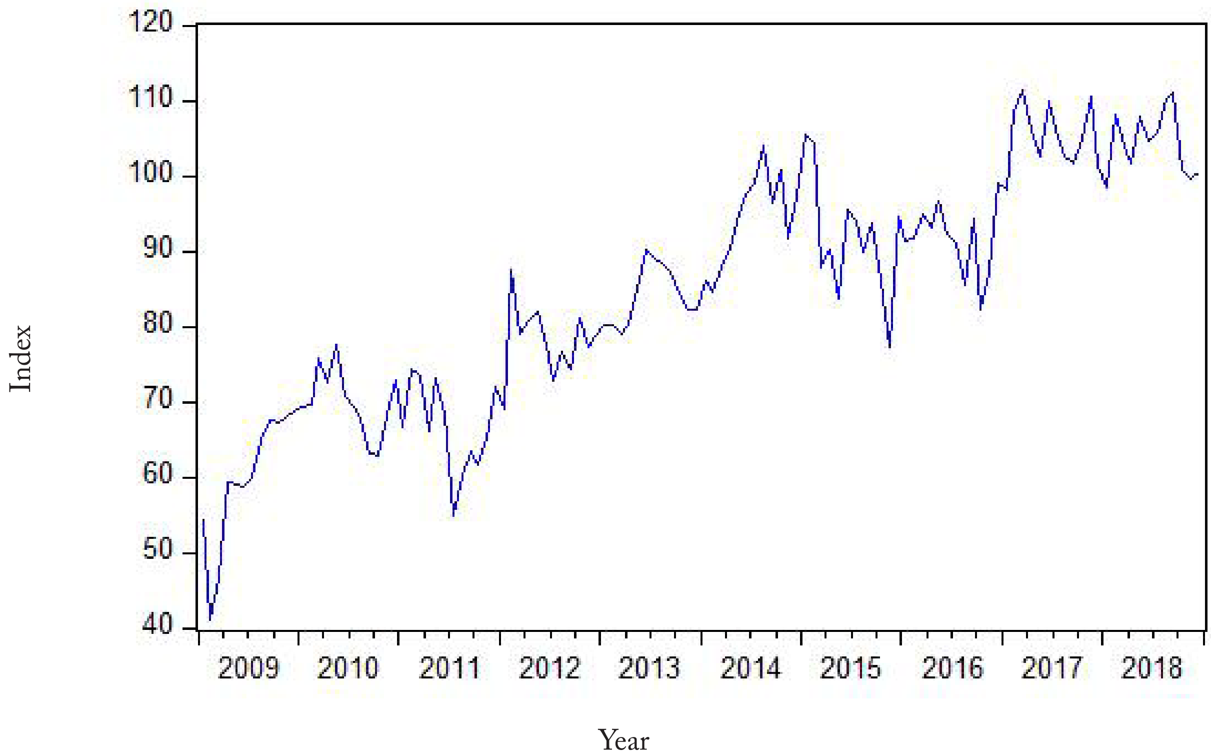
Employment of Southeast Minnesota residents declined by 0.8 percent over the year ending December 2018. The regional unemployment rate was 3.0 percent in December, slightly higher than was recorded one year earlier. Initial claims for unemployment insurance in December 2018 fell by 13.4 percent from one year earlier and the Southeast Minnesota labor force decreased by 0.7 percent. Average weekly wages in Southeast Minnesota rose by 3.9 percent over the past year. The planning area's annual bankruptcies were 14.4 percent higher than one year ago.

Data from the Rochester area—the largest market in Southeast Minnesota—were mixed. An increase in overall employment (and job gains in the area's manufacturing and health/education sectors), a larger labor force, and lower initial jobless claims contributed to a favorable outlook for the region. Fewer overall new business filings, lower average hourly earnings, a reduction in average weekly work hours, and a smaller valuation of residential building permits in the Rochester area were negative indicators.

SOUTHEAST MINNESOTA LEADING ECONOMIC INDICATORS INDEX

The SCSU Southeast Minnesota Leading Economic Indicators (LEI) index is designed to predict performance of the regional economy with a four-to-six month lead time. The LEI finished 9.81 points lower in the fourth quarter, and is now nearly unchanged from its level of one year earlier. As can be seen in the accompanying figure, the LEI has flattened out over the last several quarters as the regional economy has approached full employment. Southeast Minnesota is the one region of Minnesota that is experiencing the challenges of declining overall employment as its labor force shrinks. While long-term fundamentals appear to remain solid in this region, it should be noted that year-over-year unemployment rates were higher in December 2018 and annual bankruptcies rose at a double-digit rate. This region can expect weaker future economic growth as it adjusts to finding new sources of labor to replace its shrinking work force.

SCSU Southeast Minnesota Index of Leading Economic Indicators (December 1999 = 100)



Components of SCSU Southeast Minnesota Leading Economic Indicators Index

Component of Index	Contribution to LEI, 4th quarter 2018	Contribution to LEI, 3rd quarter 2018
Minnesota Business Conditions Index	-2.81	0.72
Southeast Minnesota initial claims for unemployment insurance	-0.12	-0.29
Southeast Minnesota new filings of incorporation and LLCs	-2.43	2.31
Rochester MSA residential building permits	-3.37	1.92
Consumer Sentiment, University of Michigan	-1.07	1.13
TOTAL CHANGE	**-9.81**	**5.80**

All five components of the LEI had a negative reading in the fourth quarter. A decline in Rochester area residential building permits and weaker consumer sentiment helped drag down the leading index in the current period. A reduction in new filings of incorporation and LLC also caused the LEI to move lower. The Minnesota Business Conditions Index (compiled by Creighton University), which serves as a general measure of statewide business conditions, also contributed a negative value to this quarter's index.

SCSU Southeast Minnesota Leading Economic Indicators Index

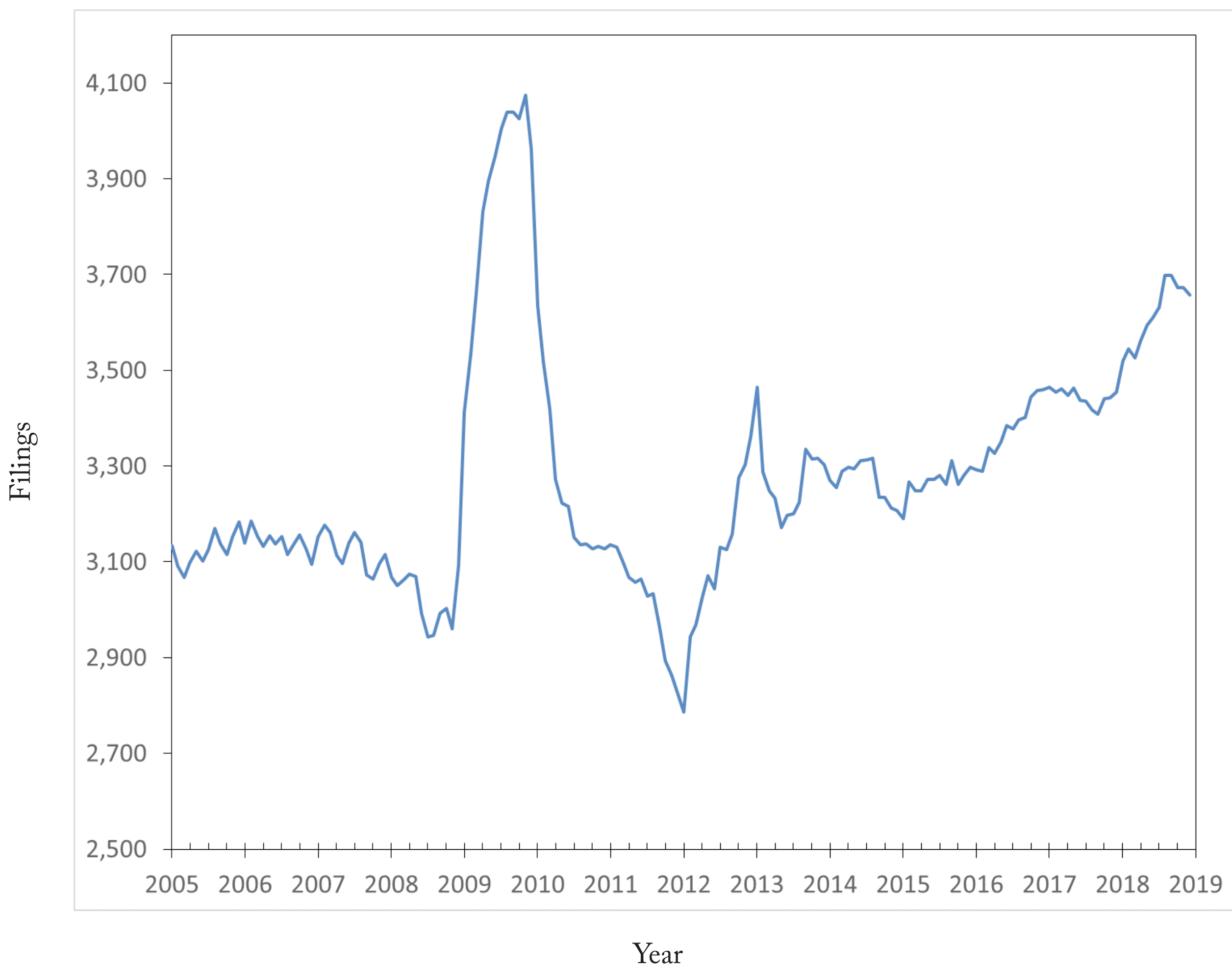
	2018	2017	Percentage change
Minnesota Business Conditions Index December	55.5	56.8	-2.3%
Southeast Minnesota initial claims for unemployment insurance December	2,249	2,598	-13.4%
Southeast Minnesota new filings of incorporation and LLCs Fourth Quarter	568	575	-1.2%
Rochester MSA single-family building permits December	27	35	-22.9%
Consumer Sentiment, University of Michigan December	98.3	95.9	2.5%
Southeast Minnesota Leading Economic Indicators Index December (December 1999 = 100)	104.6	104.4	0.2%

SOUTHEAST MINNESOTA BUSINESS FILINGS

Fourth quarter new business filings fell 4.7 percent to a level of 804. As can be seen in the accompanying graph, the 12-month moving total of new business filings in Southeast Minnesota has generally trended upward since the beginning of 2012, so these numbers will be closely watched in future quarters. The abrupt increase in new filings in the middle of 2008 is largely a result of increased new LLC filings. This outlier (resembling a shark fin) is related to considerably higher filings in the construction industry due to legal and regulatory issues and appears to be a one-time only transitory event seen in the data in all regions of Minnesota.

Note: The graphs in this section show the 12-month moving total for the various new business filings in Southeast Minnesota that are registered with the Office of the Minnesota Secretary of State. Doing so removes seasonal patterns in the data.

Total New Business Filings—Southeast Minnesota Planning Area (12-month moving total)



Quarter	IV: 2017	I: 2018	II: 2018	III: 2018	IV: 2018	2018 Quarter IV: Percent change from prior year
Southeast Minnesota Total New Business Filings	844	1,004	970	880	804	-4.7%

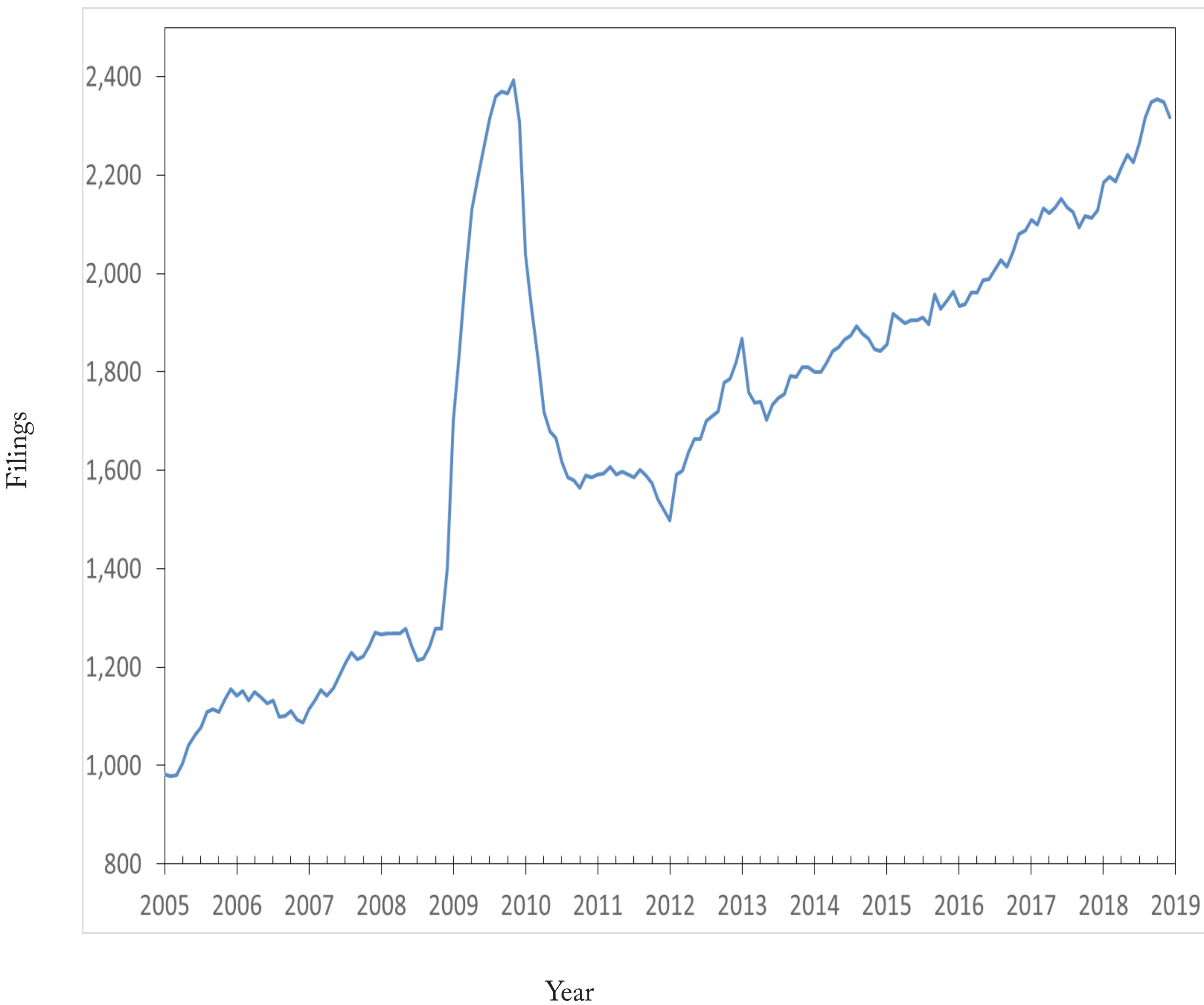
After levelling off for nearly five years, the moving total of new business incorporations once again began to slowly trend downward in Southeast Minnesota at the end of 2016. However, the moving total of new incorporations leveled out in the first three quarters of 2018. The fourth quarter saw a surge of new filings for incorporation in the region as the series jumped by 48.9 percent compared to one year earlier.

New Incorporations—Southeast Minnesota Planning Area
(12-month moving total)

Quarter	IV: 2017	I: 2018	II: 2018	III: 2018	IV: 2018	2018 Quarter IV: Percent change from prior year
Southeast Minnesota New Business Incorporations	47	64	53	49	70	48.9%

There has been a move in Southeast Minnesota, as in all of the state, away from the traditional incorporation form of business organization towards the LLC. While new business incorporations remain an important indicator of new business formation in Southeast Minnesota, LLCs are increasingly useful in evaluating regional economic performance. As seen below, there is a considerable upward trend in LLCs in Southeast Minnesota. With the exception of the outlier period in 2008-2009, new LLC formation has shown a fairly steady rate of growth since 2005. Fourth quarter LLC filings fell by 5.7 percent over their year earlier level as the 12-month moving total of this series turned downward.

New Limited Liability Companies—Southeast Minnesota Planning Area (12-month moving total)



Quarter	IV: 2017	I: 2018	II: 2018	III: 2018	IV: 2018	2018 Quarter IV: Percent change from prior year
Southeast Minnesota New Limited Liability Companies	528	643	594	583	498	-5.7%

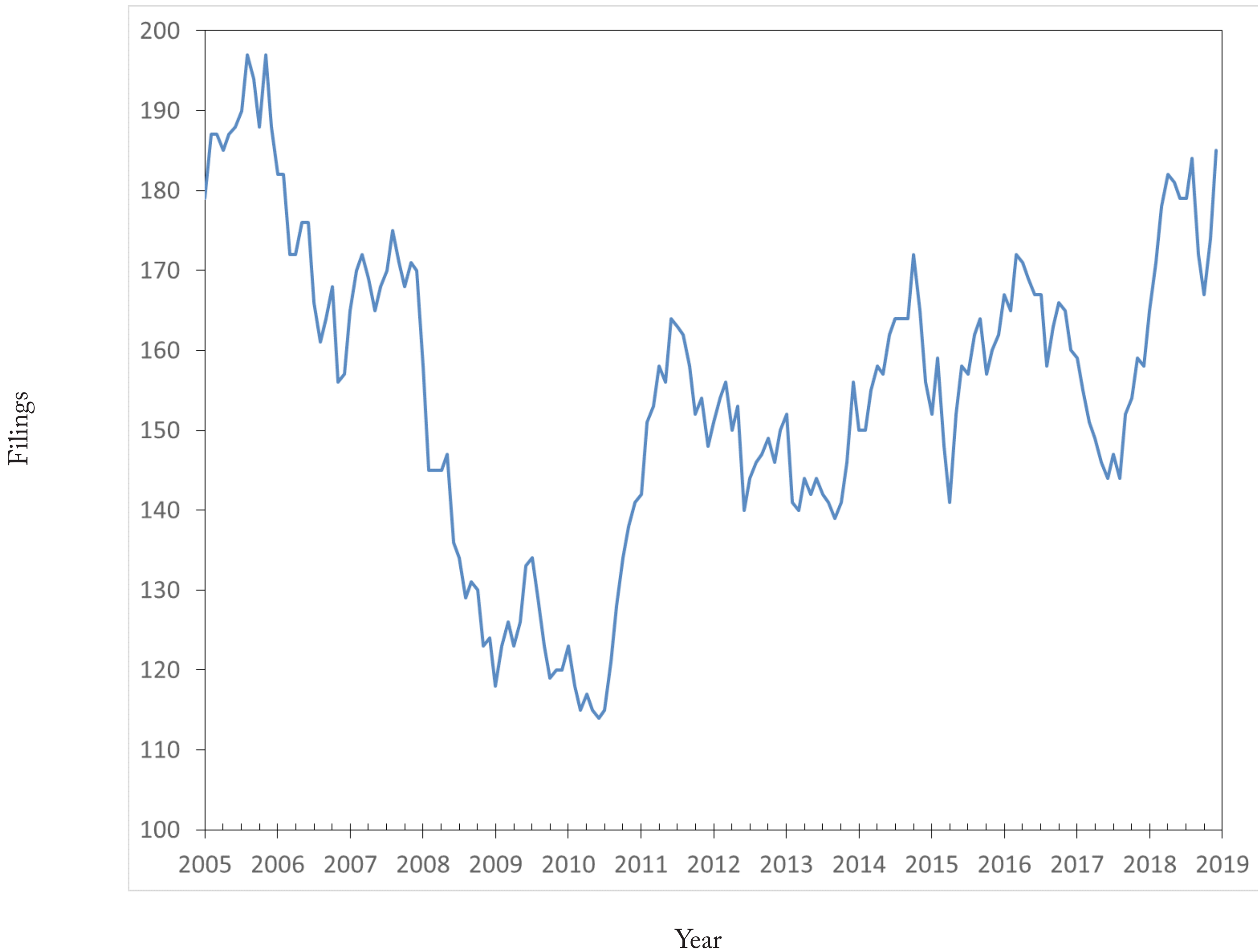
On a year over year basis, assumed names, which include sole proprietors or organizations that do not have limited liability, fell by 20.2 percent in Southeast Minnesota in the fourth quarter. As can be seen in the accompanying graph, other than a period of decline in 2016-17, this series had been trending upward since the beginning of 2015. However, the moving total of assumed names has declined over the past two quarters in this region. The series remains well below the level observed 10 years ago.

New Assumed Names—Southeast Minnesota Planning Area (12-month moving total)

Quarter	IV: 2017	I: 2018	II: 2018	III: 2018	IV: 2018	2018 Quarter IV: Percent change from prior year
Southeast Minnesota New Assumed Names	228	246	283	208	182	-20.2%

The moving total of new Southeast Minnesota non-profits registered with the Office of the Minnesota Secretary of State has been volatile over the past several years. As can be seen in the accompanying graph, this series had turned downward since the beginning of 2016, but has recently moved upward. The number of newly formed non-profits totaled 54 in the recent quarter (a 31.7 percent increase over the fourth quarter of 2017).

New Non-Profits—Southeast Minnesota Planning Area (12-month moving total)



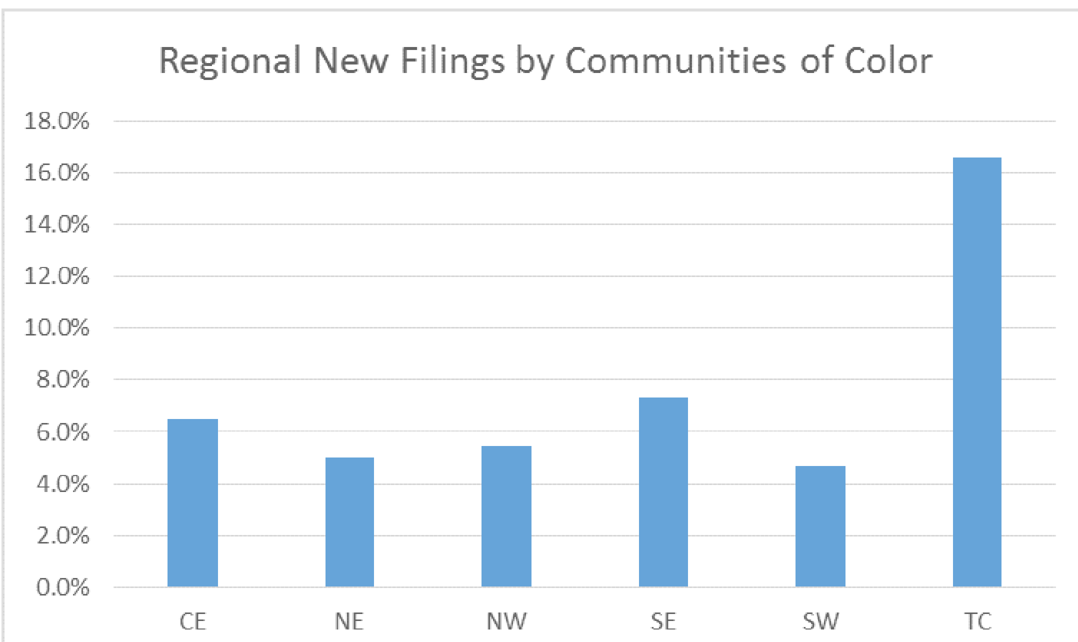
Quarter	IV: 2017	I: 2018	II: 2018	III: 2018	IV: 2018	2018 Quarter IV: Percent change from prior year
Southeast Minnesota New Non-Profits	41	51	40	40	54	31.7%

MINNESOTA BUSINESS SNAPSHOT SURVEY RESULTS

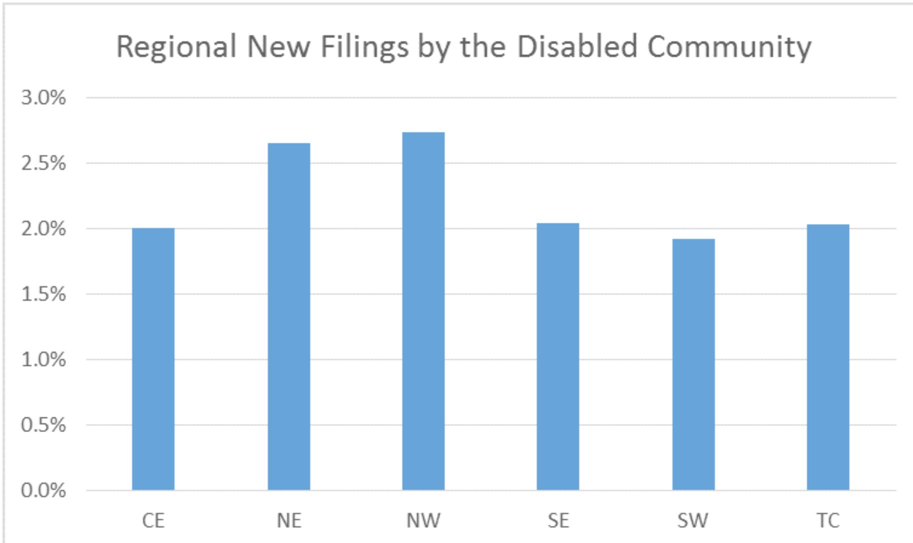
In Fall 2016, the Office of the Minnesota Secretary of State initiated a short voluntary survey (known as Minnesota Business Snapshot) for both new and continuing business filers. Questions found in the survey address basic questions related to the background of business filers, industry classification, employment levels and annual revenue of the filer, and whether the business is a full- or part-time activity for the filing entity. While a comprehensive analysis of this promising new data set is the beyond the scope of this regional economic and business conditions report, the survey results do provide useful additional background information to complement the business filing data.

To match up the Minnesota Business Snapshot (MBS) information with the data analyzed in this report, only surveys accompanying new filings in the fourth quarter of 2018 are analyzed. For the entire State of Minnesota, the overall response rate for this voluntary survey is approximately 59 percent. This yields thousands of self-reported records in this emerging data set. For Southeast Minnesota, 61 percent of new business filers also completed at least some portion of the MBS survey. The results are reported in this section.

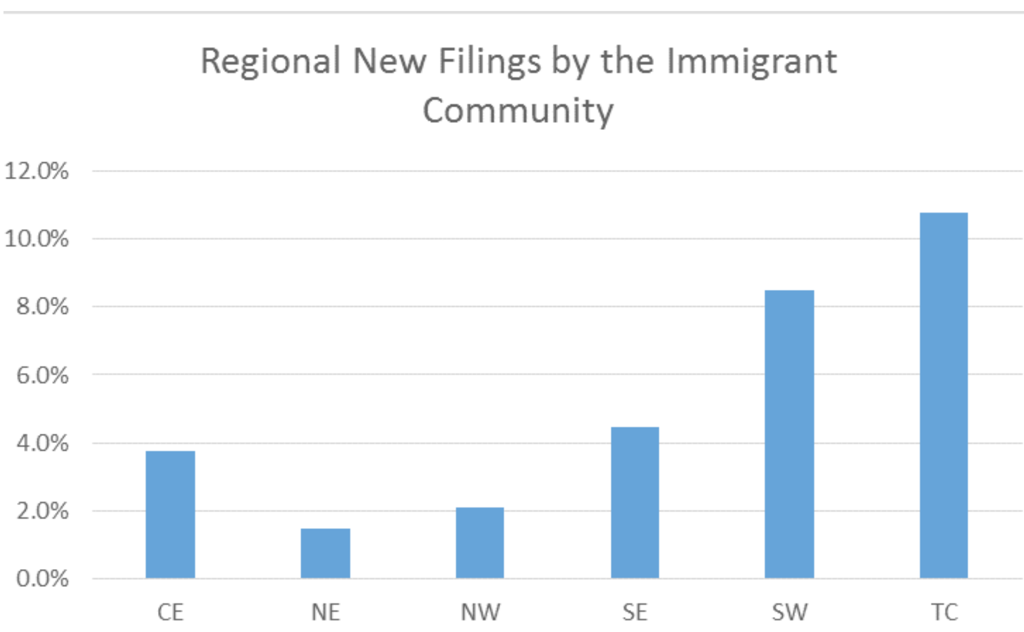
About 7.3 percent of those new filers completing the MBS from the Southeast Minnesota planning area report being from a community of color. This is a considerably lower percentage than in the Twin Cities, but is higher than all other outstate regions of Minnesota.



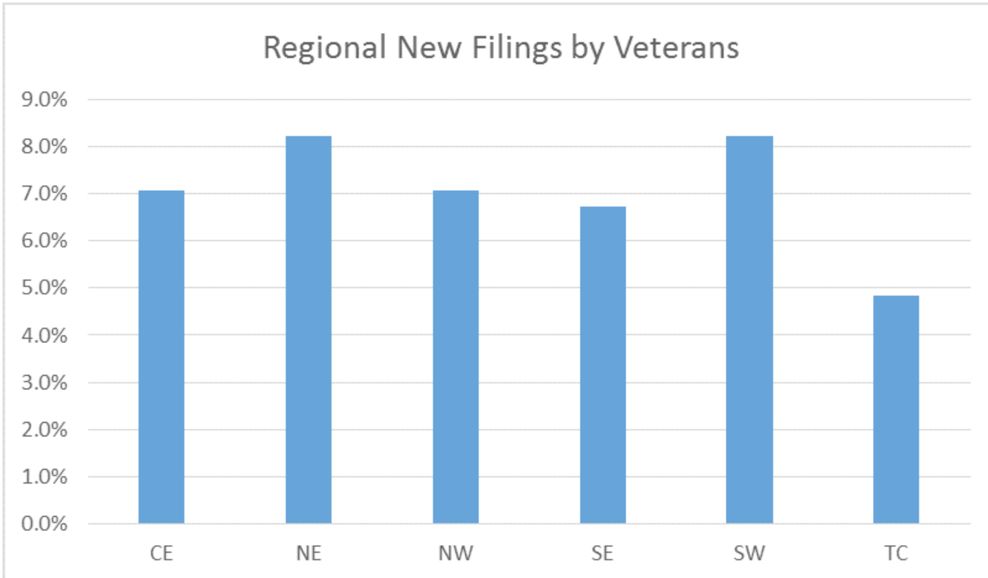
Only 2 percent of Southeast Minnesota's new filers are from the disability community.



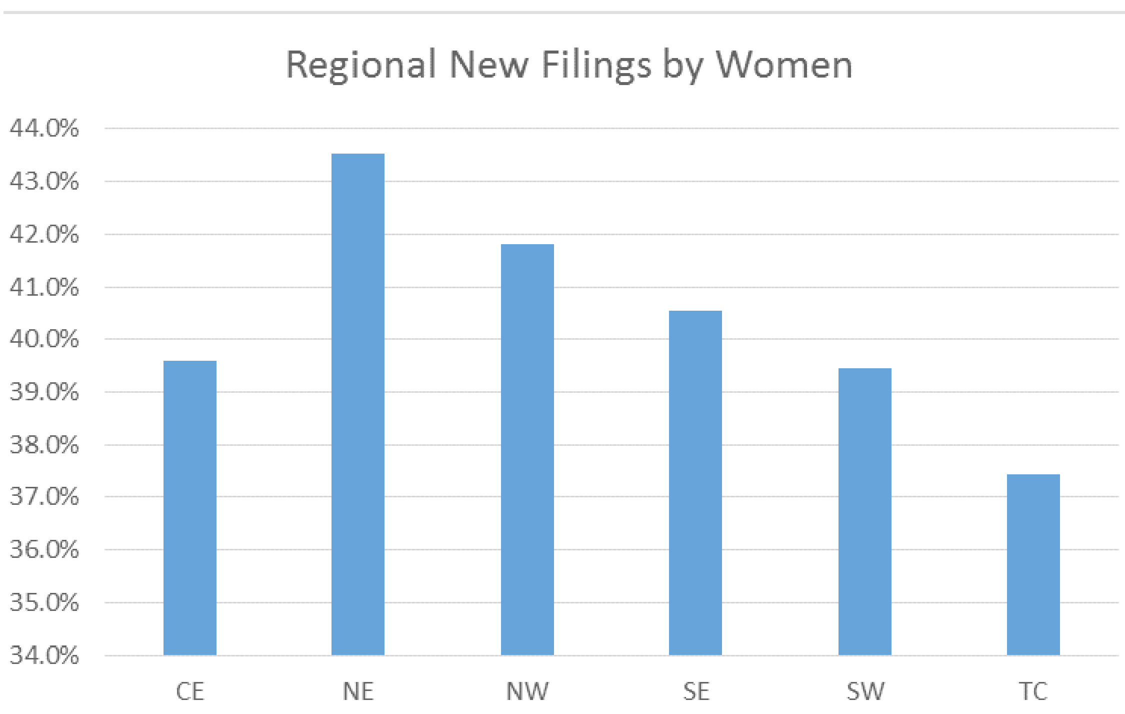
4.5 percent of new business filings in Southeast Minnesota come from the immigrant community. This is a larger percentage than is found in most other portions of the state.



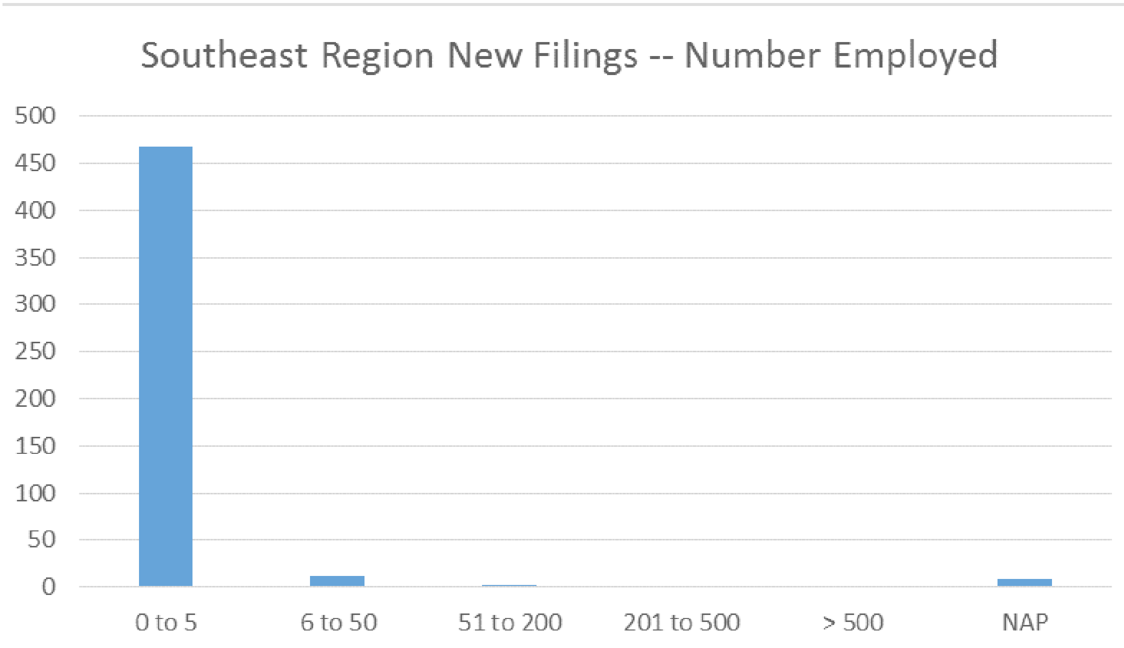
6.7 percent of new filings in Southeast Minnesota come from military veterans.



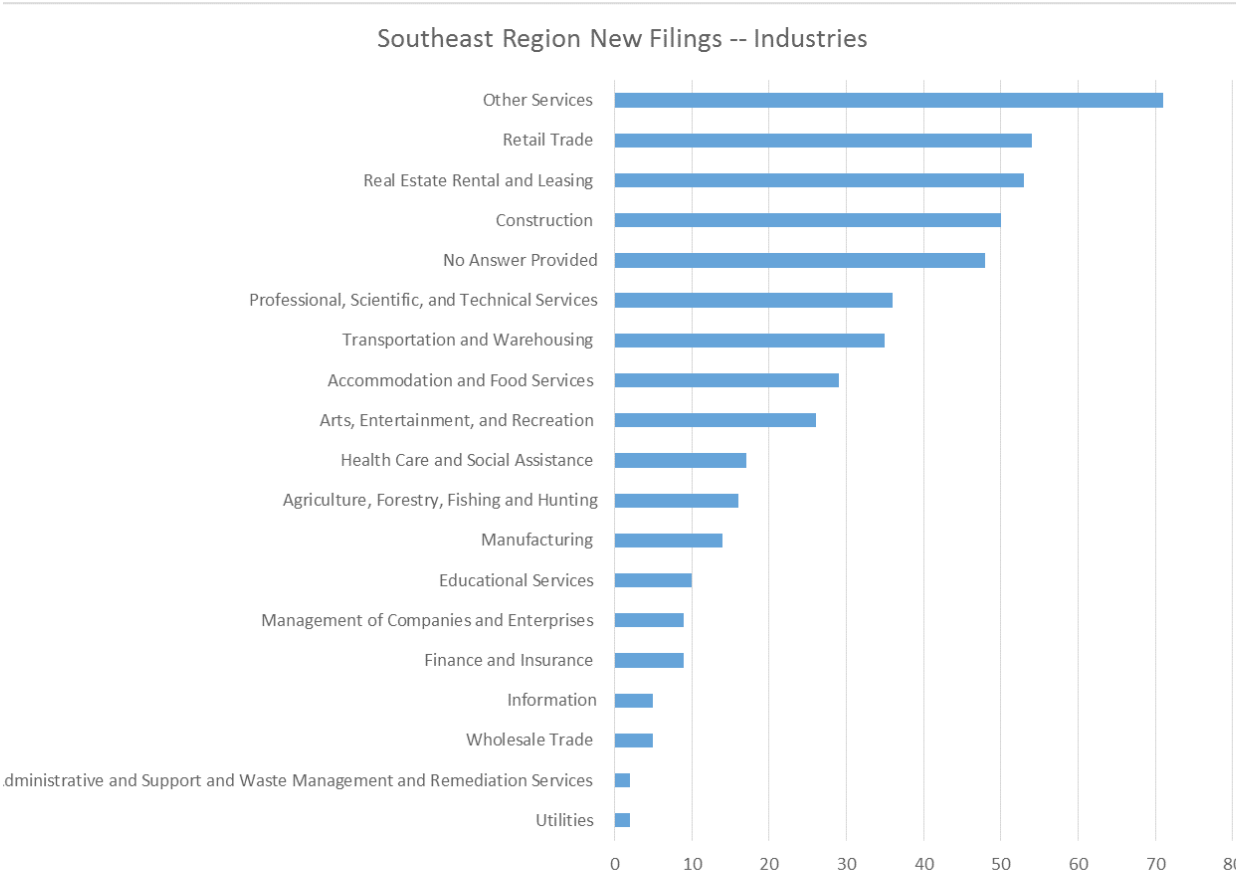
Woman owners represented 40.5 percent of the new business filings in Southeast Minnesota in the fourth quarter of 2018.



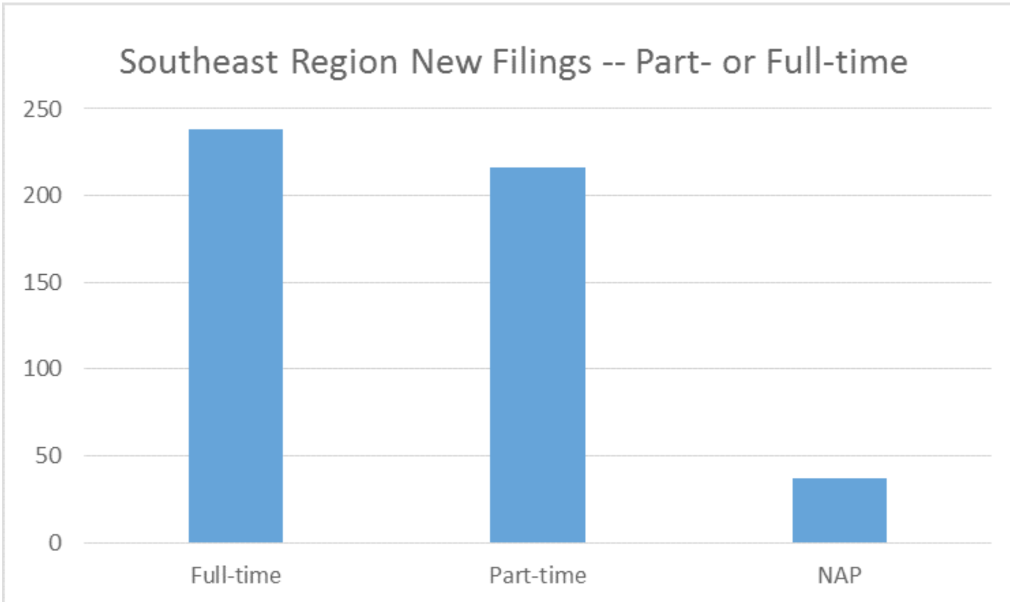
While not all of those participating in the survey completed all portions of the Minnesota Business Snapshot (those not responding to a particular question are represented in this section by “NAP”—no answer provided), 482 responses were tallied to a question asking the new business filer to indicate the range of employment at the business. As expected, most new businesses start small—employment at most companies submitting a new filing ranges from 0-5 employees.



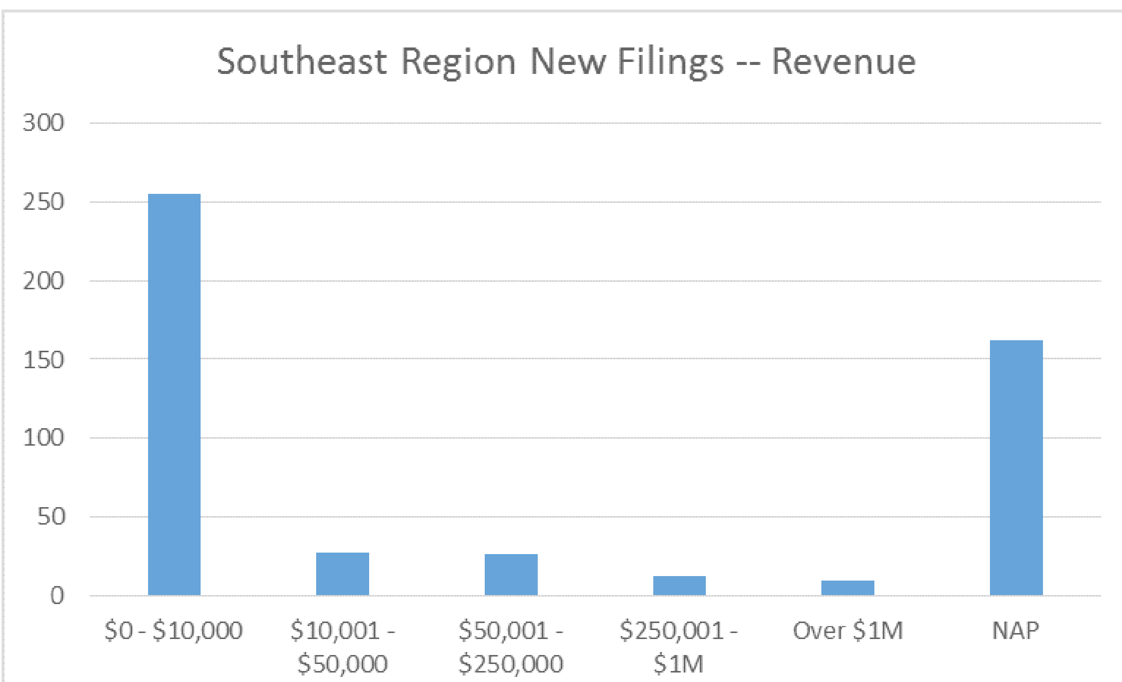
Using the North American Industry Classification System (NAICS), businesses submitting new filings were asked to identify the industry in which their company was operating. While a range of industries were reported, retail trade, construction, real estate/rental/leasing and "other services" lead the way. Since businesses are often unsure of their industrial classification, the "other services" category is likely to represent a "catch-all" category for service-related businesses who were unable to specify their industry. Forty-eight new firms did not provide an answer to this survey item (see "NAP")



47.6 percent of those new business filers who filled out a response on the MBS survey on full- and part-time business ownership status report they are part-time business owners



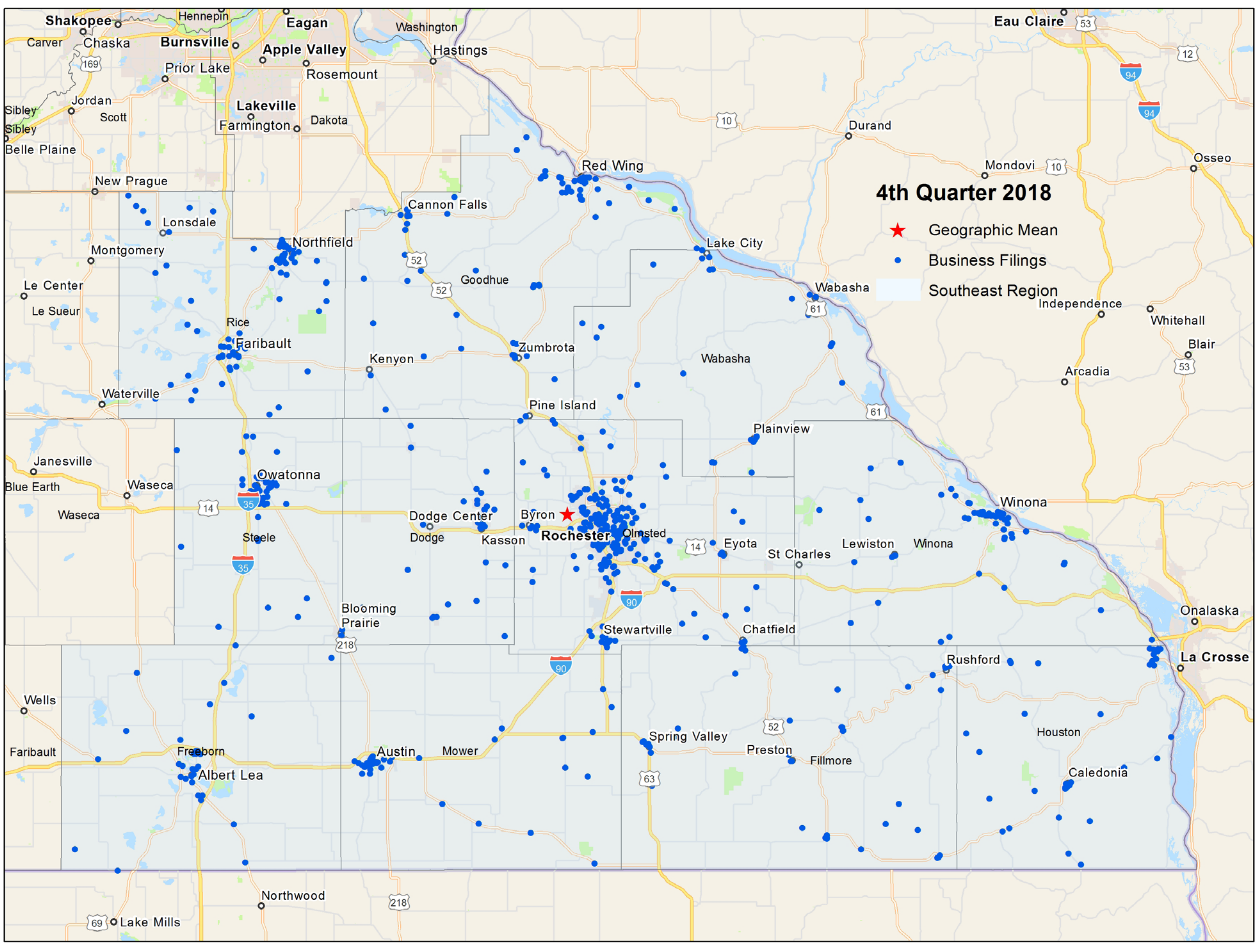
162 new filers in Southeast Minnesota did not provide an answer to the MBS item that asked them to report the company's revenue. Of those businesses that answered the question, the largest share report revenues less than $10,000. Forty-seven firms report annual revenues in excess of $50,000.



MAPS

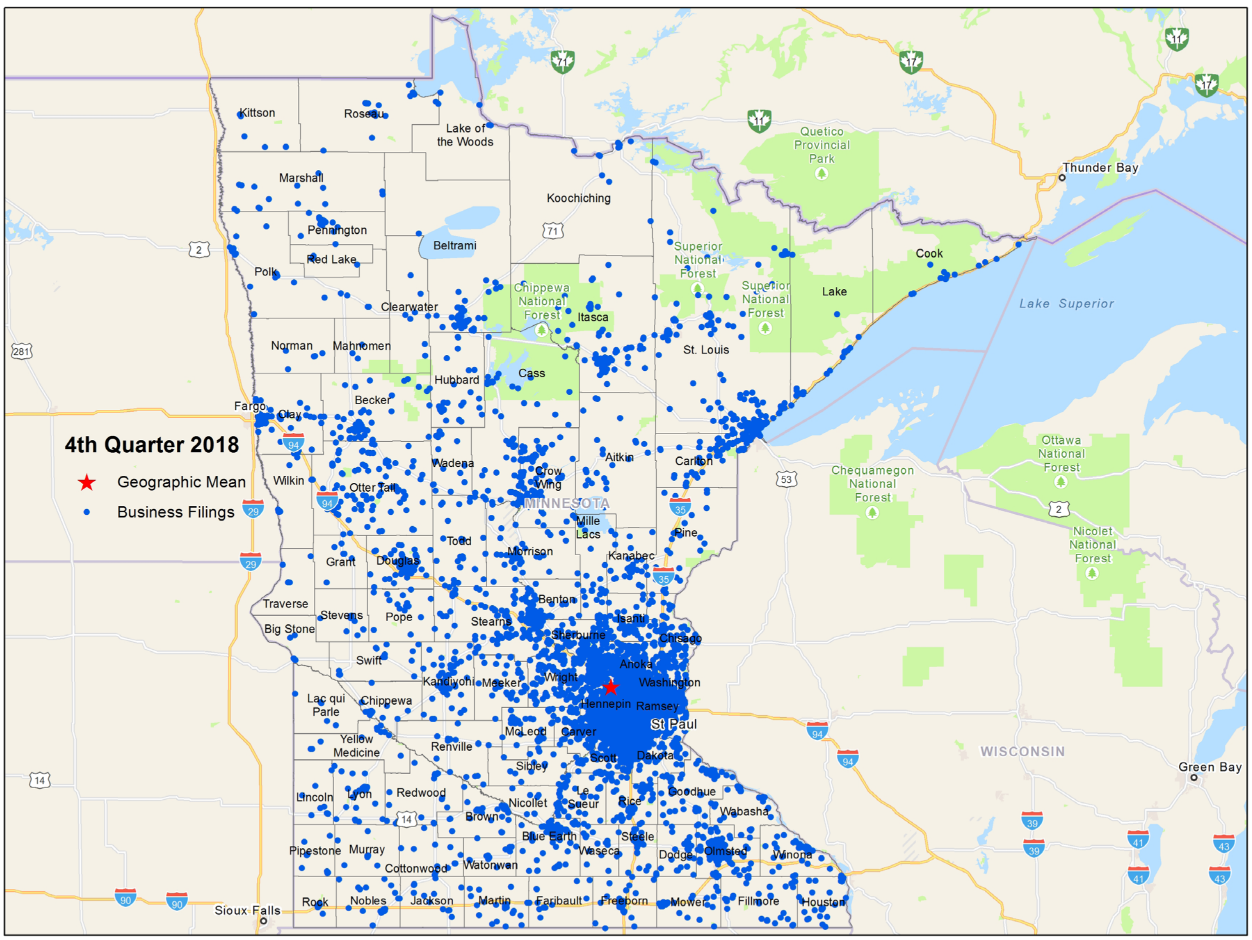
The first map shown below is a visual representation of new business filings around the Southeast Minnesota planning area in the fourth quarter of 2018. The densest areas of new business formation are in the Rochester metro. Owatonna, Faribault, Northfield, Albert Lea, Austin, Winona, and Red Wing also generated multiple new business filings. Well-traveled roadways are also a predictor of new business formation in Southeast Minnesota.

Southeast Minnesota Planning Area--New Business Formation--Quarter 4: 2018



The second map shows new business filings for the state as a whole. This visual aid demonstrates the considerable extent to which the Twin Cities metro area dominates new business formation in the state. The map shows how the Twin Cities metro stretches along roadways into the Southeast, Southwest and Central planning areas. The map demonstrates the importance of cities and roadways in encouraging economic development. St. Cloud now appears to be integrated into the Twin Cities metro as the I-94/US-10 corridor continues to be a magnet for new business formation. There is also considerable new business formation in the southern part of the state, particularly in Rochester and between the Twin Cities and Mankato. The importance of Interstates 90, 94, and 35 as well as US-10 and MN 61 (along the North Shore) in new business filings is also easily seen in this map.

Minnesota--New Business Formation--Quarter 4: 2018

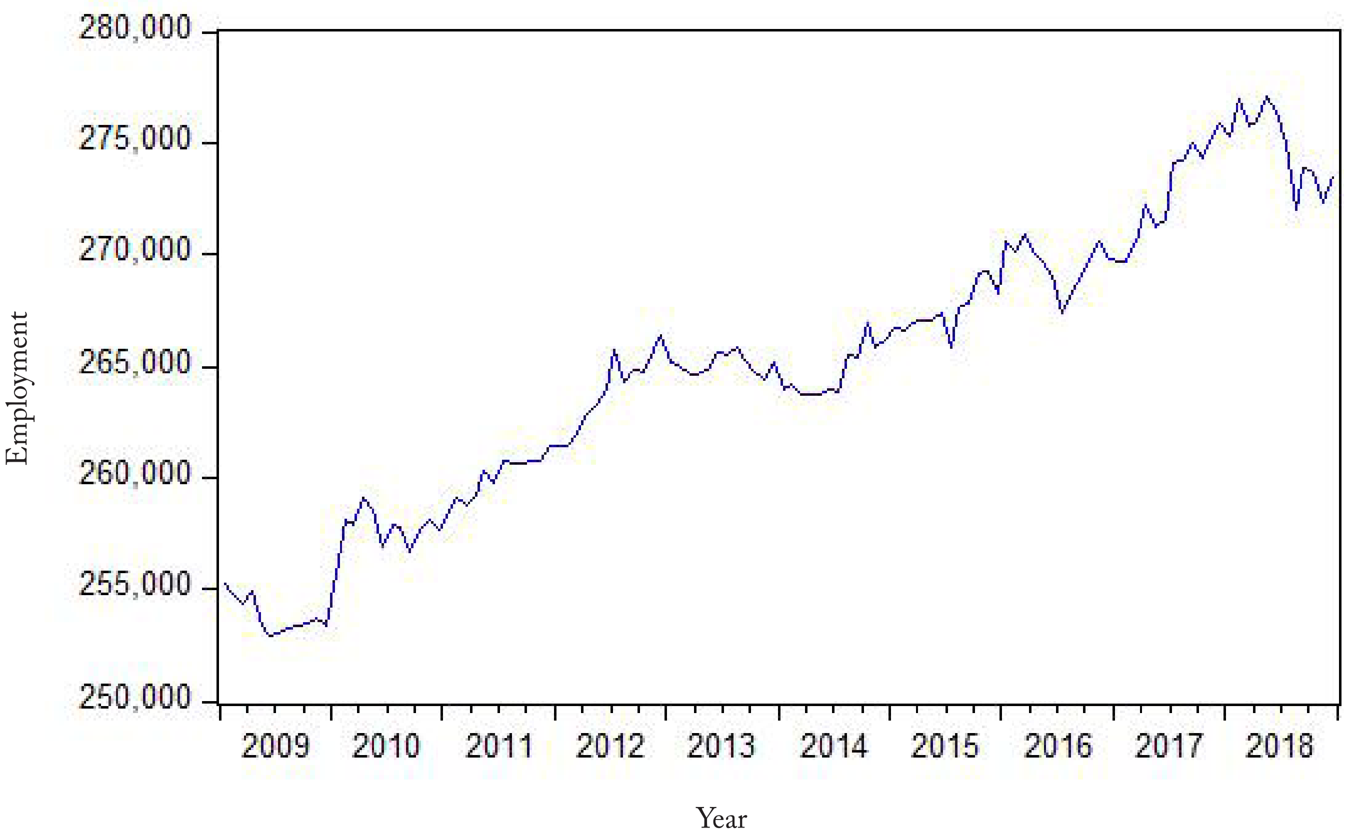


SOUTHEAST MINNESOTA LABOR MARKET CONDITIONS

Employment of those living in the Southeast Minnesota planning area contracted by 0.8 percent over the past year as the planning area appears to have reached full employment and its labor force has begun to decline. As shown in the accompanying graph, the 12-month moving average of total employment had been trending upward (with some brief interruptions) since the end of the Great Recession, but has declined in recent months.

Note: seasonally adjusted labor market data are typically not available to evaluate regional economic performance so some series have been created to illustrate seasonal patterns of the regional labor market. Graphs of these indicators are found in this section of the report. Tabular data are not seasonally adjusted.

Employment—Southeast Minnesota Planning Area (12-month moving average)



Month	December 2017	July 2018	August 2018	September 2018	October 2018	November 2018	December 2018
Employment (Not seasonally adjusted)	275,536	278,194	272,916	273,535	275,795	273,681	273,392

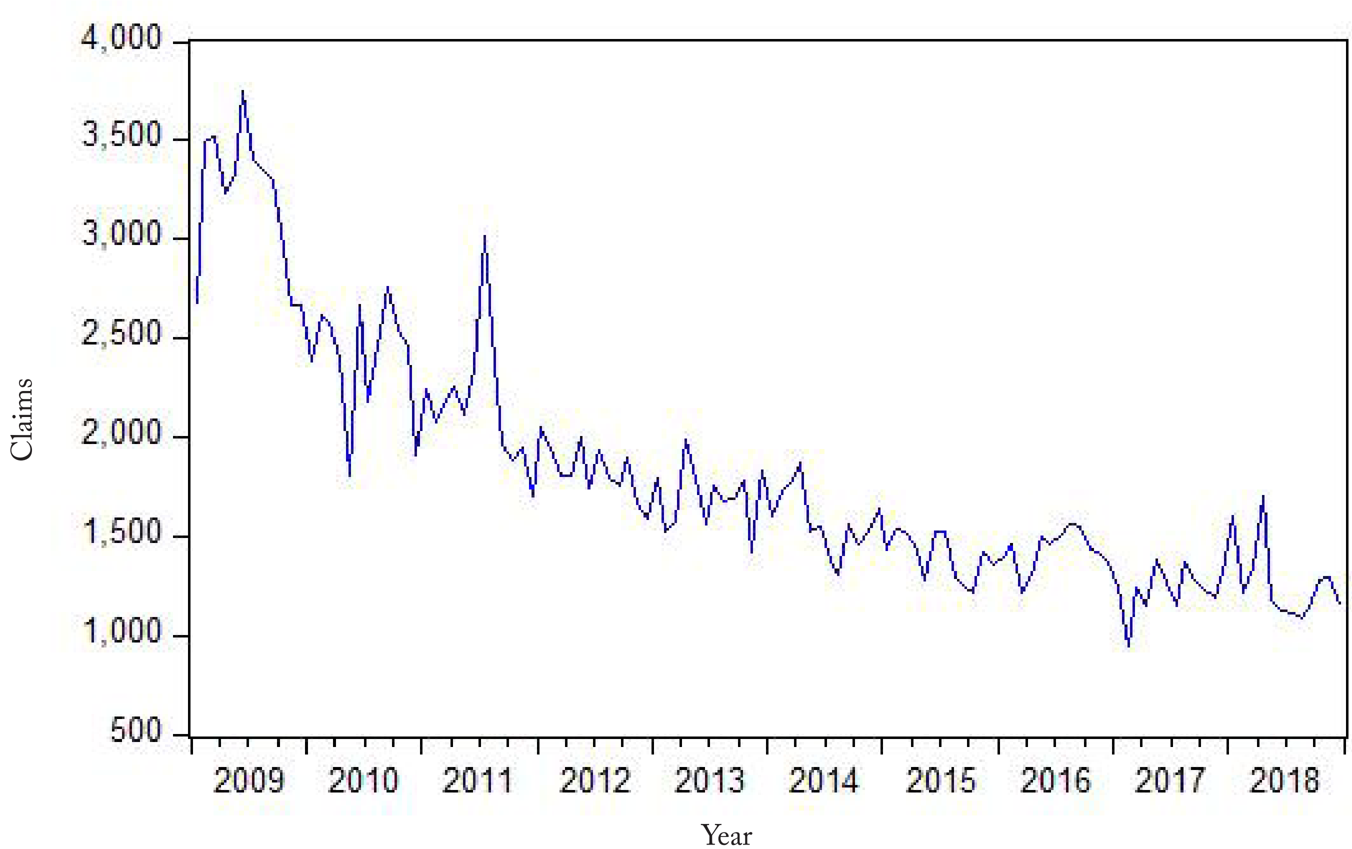
After a long-term decline, the seasonally adjusted unemployment rate in Southeast Minnesota started to rise in the fourth quarter. The non-seasonally adjusted unemployment rate also inched up relative to one year earlier. This increase in the measured unemployment rate may be caused by a declining labor force in this region of the state.

Unemployment Rate, seasonally adjusted—Southeast Minnesota Planning Area

Month	December 2017	July 2018	August 2018	September 2018	October 2018	November 2018	December 2018
Unemployment Rate (Not seasonally adjusted)	2.9%	2.5%	2.4%	2.1%	2.0%	1.9%	3.0%

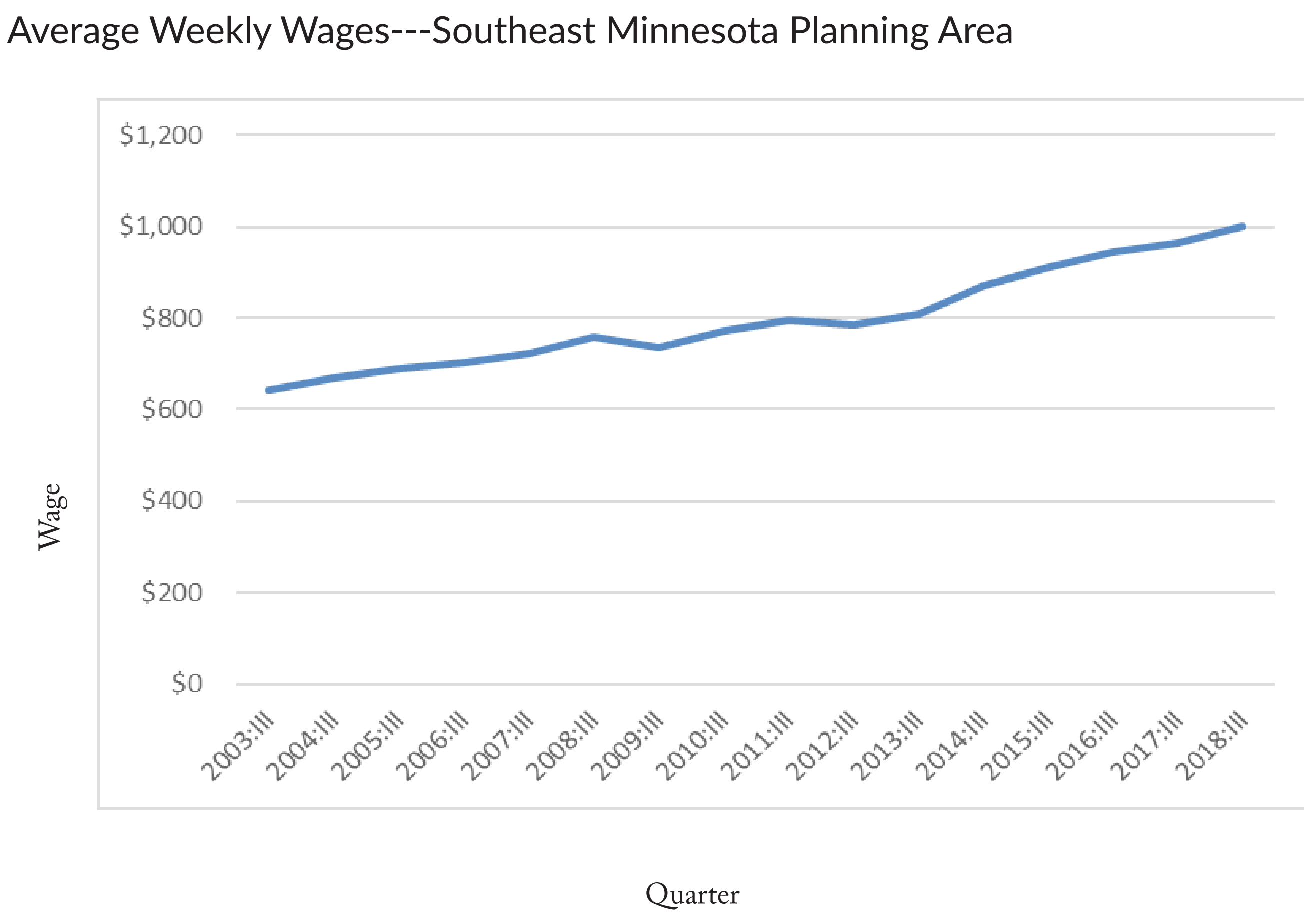
New claims for unemployment insurance in December 2018 were 13.4 percent lower than one year earlier. On a seasonally adjusted basis, these claims have leveled out for the last several quarters.

Total Initial Claims for Unemployment Insurance, seasonally adjusted—Southeast Minnesota Planning Area



Period	December 2017	July 2018	August 2018	September 2018	October 2018	November 2018	December 2018
Initial claims (Not seasonally adjusted)	2,598	808	699	733	990	2,203	2,249

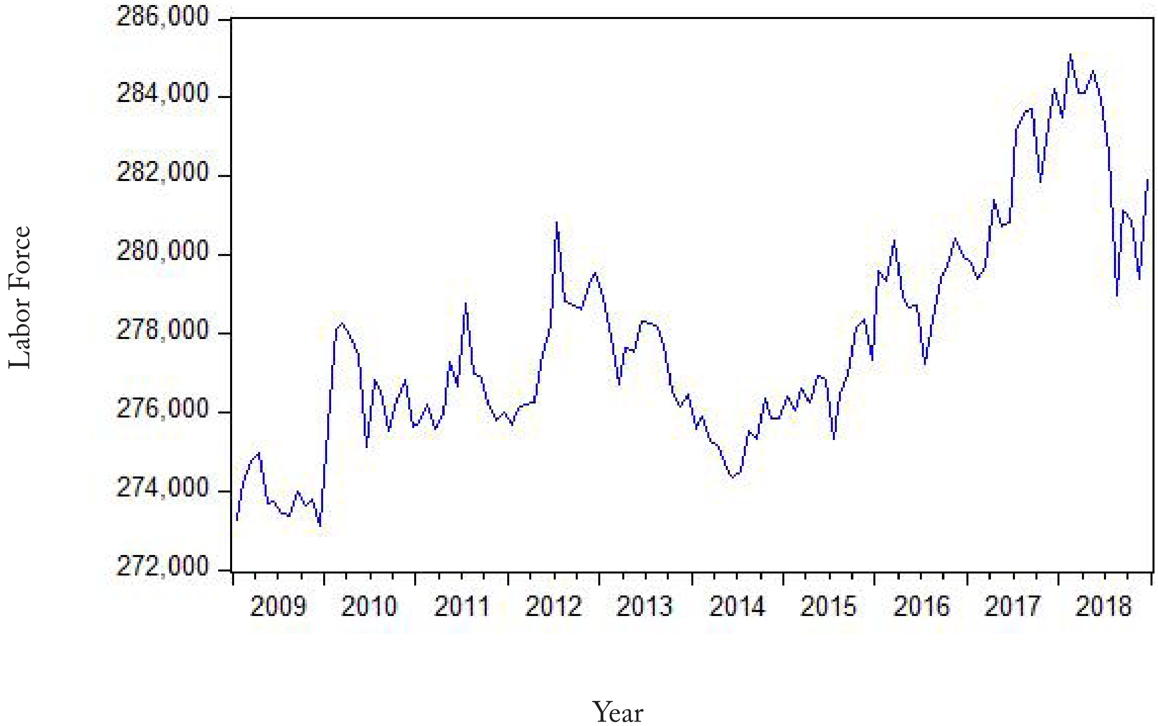
With continuing labor shortages being reported across the state, it is no surprise that there is upward pressure on wages. At $1,001, the average weekly wage in Southeast Minnesota in the third quarter of 2018 was 3.9 percent above its level of one year earlier. Wages are increasing throughout Minnesota. Note that the average weekly wage in Southeast Minnesota is second highest among Minnesota's six planning areas. Only the Twin Cities (with a current average weekly wage of $1,184) offers higher earnings.



Quarter	2013:III	2014:III	2015:III	2016:III	2017:III	2018:III
Average Weekly Wages	$808	$872	$910	$945	$963	$1,001

The Southeast Minnesota labor force decreased by 0.7 percent over the past year. The 12-month moving average of the regional labor force had steadily increased since the beginning of 2014, but experienced a precipitous decline in recent 2018.

Labor Force—Southeast Minnesota Planning Area (12-month moving average)

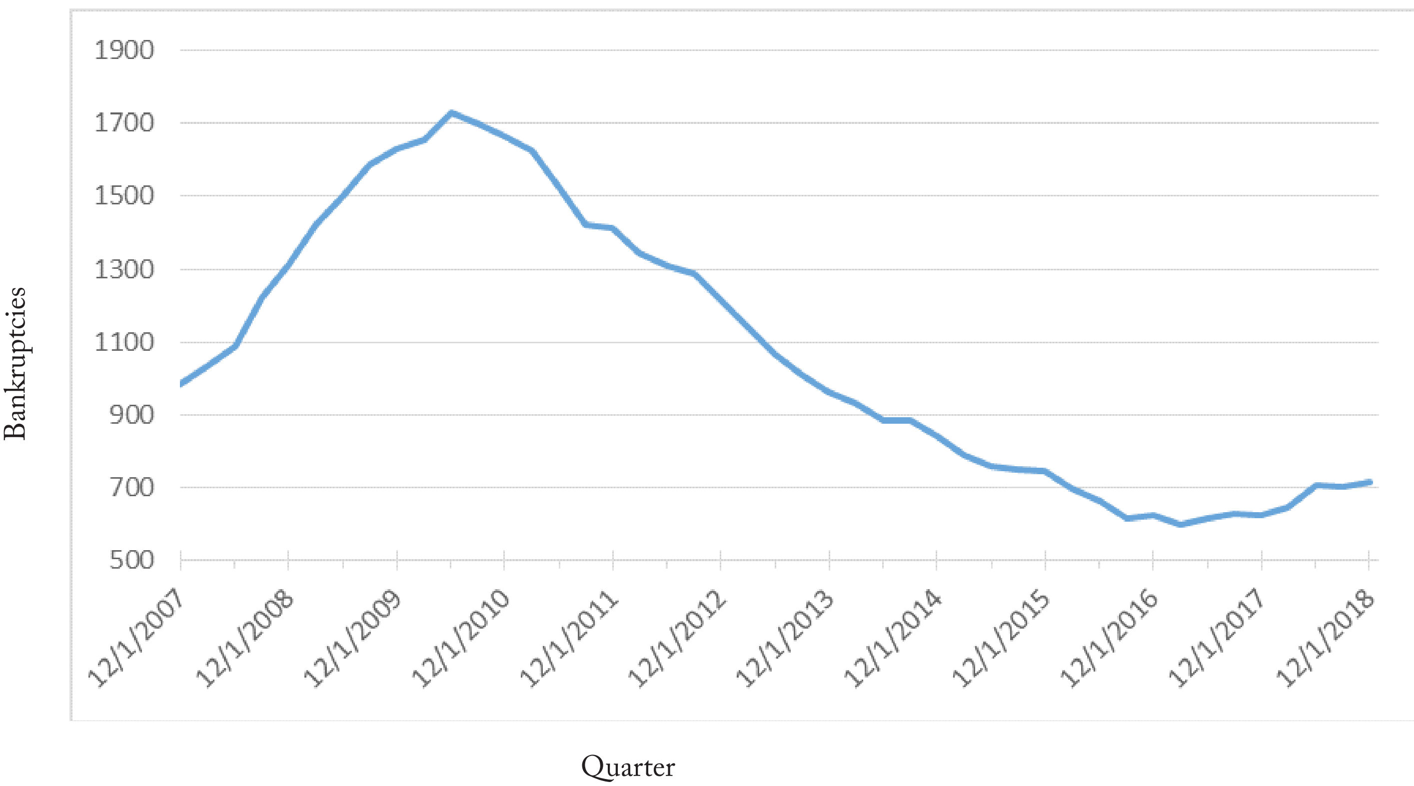


Year (December)	2013	2014	2015	2016	2017	2018
Labor Force (Not seasonally adjusted)	275,374	274,907	276,596	279,386	283,818	281,704

SOUTHEAST MINNESOTA BANKRUPTCIES

The figure below shows the 12-month moving total for Southeast Minnesota bankruptcies since the second quarter of 2007 (shortly before the beginning of the Great Recession). As can be seen in the figure, this moving total increased through the second quarter of 2010, and steadily declined until the end of 2016. Annual bankruptcies in this region bottomed out in 2017 and have now started to rise. With 703 bankruptcies over the past twelve months, annual bankruptcies in Southeast Minnesota are now more than 11 percent above their level of one year ago.

Southeast Minnesota Bankruptcies (12-month moving total)



Year (Fourth Quarter)	2013	2014	2015	2016	2017	2018
Annual Bankruptcies (not seasonally adjusted)	963	843	746	623	624	714

ECONOMIC INDICATORS

Rochester MSA Indicators	Period Covered	Current Period	Prior Year	Annual Percent Change		Long-Term Average (since 1999, unless noted)	
Labor Market							
Employment	December 2018 (m)	123,004	121,368	1.3%	↑	0.9%	
Manufacturing Employment	December 2018 (m)	10,800	10,351	4.3%	↑	-2.4%	
Educational and Health Employment	December 2018 (m)	50,988	49,963	2.1%	↑	2.7%	
Average Weekly Work Hours--Private Sector	December 2018 (m)	32.2	34.1	-5.6%	↓	33.2	(since 2006)
Average Earnings Per Hour--Private Sector	December 2018 (m)	$33.67	$36.53	-7.8%	↓	1.6%	(since 2007)
Unemployment Rate	December 2018 (m)	2.8%	2.8%	NA	↔	3.8%	
Labor Force	December 2018 (m)	120,953	119,391	1.3%	↑	0.6%	
Initial Jobless Claims	December 2018 (m)	860	972	-11.5%	↓	NA	
Business Formation							
Total New Business Filings	Fourth Quarter 2018 (q)	406	431	-5.8%	↓	349	(since 2000)
New Business Incorporations	Fourth Quarter 2018 (q)	35	15	133.3%	↑	47	(since 2000)
New Limited Liability Companies	Fourth Quarter 2018 (q)	253	281	-10.0%	↓	175	(since 2000)
New Assumed Names	Fourth Quarter 2018 (q)	87	112	-22.3%	↓	107	(since 2000)
New Non-Profits	Fourth Quarter 2018 (q)	31	23	34.8%	↑	20	(since 2000)
Rochester Residential Building Permit Valuation	December 2018 (m)	7,906	9,323	-15.2%	↓	NA	

(m) represents a monthly series
(q) represents a quarterly series

Southeast Minnesota contains the Rochester MSA, an area that derives much of its employment from the educational and health sector. This sector continues to be a pillar of economic vitality for Rochester (and for Southeast Minnesota) as employment in the educational/health sector grew 2.1 percent over the twelve-month period ending in December 2018. Note that the share of employment in Rochester's educational and health sector has increased from 29.7 percent in December 1999 to 41.5 percent today, so this sector is vital to economic growth in the Rochester MSA. The overall number of new business filings contracted by 5.8 percent as new LLC filings fell 10 percent over the year ending in the fourth quarter of 2018. The value of residential building permits fell in the Rochester area and average weekly work hours and hourly earnings contracted. The MSA unemployment rate was steady as the labor force grew. Initial jobless claims fell.

STATE AND NATIONAL INDICATORS

MINNESOTA Indicators	Dec 2018	Sep 2018	Dec 2017	Change from one quarter ago	Annual Change
Nonfarm payroll employment, SA	2,961,100	2,958,100	2,942,800	0.1%	0.6%
Average weekly hours worked, private sector	34.1	34.4	33.9	-0.9%	0.6%
Unemployment rate, seasonally adjusted	2.9%	2.8%	3.1%	NA	NA
Earnings per hour, private sector	$29.82	$29.38	$28.67	1.5%	4.0%
Philadelphia Fed Coincident Indicator, MN	138.54	137.84	133.48	0.5%	3.8%
Philadelphia Fed Leading Indicator, MN	0.70	1.88	1.08	-62.8%	-35.2%
Minnesota Business Conditions Index	55.5	60.0	56.8	-7.5%	-2.3%
Price of milk received by farmers (cwt)	$16.30	$17.50	$17.10	-6.9%	-4.7%
Enplanements, MSP airport, thousands	1,456.4	1,533.7	1,471.6	-5.0%	-1.0%
NATIONAL Indicators	**Dec 2018**	**Sep 2018**	**Dec 2017**	**Change from one quarter ago**	**Annual Change**
Nonfarm payroll employment, SA, thousands	150,275	149,575	147,596	0.5%	1.8%
Industrial production, index, SA	109.9	109.1	105.8	0.7%	3.9%
Real retail sales, SA, millions ($)	199,183	201,083	199,766	-0.9%	-0.3%
Real personal income less transfers, billions	13,753.9	13,533.7	13,338.5	1.6%	3.1%
Real personal consumption expenditures, bill.	13,014.5	12,965.9	12,735.6	0.4%	2.2%
Unemployment rate, SA	3.9%	3.7%	4.1%	NA	NA
New building permits, thousands of units	95.4	99.4	94.8	-4.0%	0.6%
Standard and Poor's 500 stock price index	2,567.3	2,901.5	2,664.3	-11.5%	-3.6%
Oil, price per barrel in Cushing, OK	$49.52	$70.23	$57.88	-29.5%	-14.4%

Economic performance found in the State and National Indicators table are mixed. For the state as a whole, there was growth in employment and improved earnings over the past year (as well as in the fourth quarter). Minnesota's seasonally adjusted unemployment rate was lower than one year ago, but inched up in the fourth quarter. Only one of the three state indicators series reported in the table were improved over the past twelve months. Milk prices fell and enplanements at the Minneapolis-St. Paul airport are lower than one year ago.

The national economic indicators found in the table are also mixed. While employment, income, industrial production and consumer spending are all improved, other measures suggest slowing national economic growth. For example, the seasonally adjusted national unemployment rate was higher in December than three months earlier and end-of-the year stock prices were lower (although they have rebounded in the first quarter of 2019). Retail sales weakened, building permits were sluggish and oil prices were also lower.

The Southeast Minnesota Quarterly Economic and Business Conditions Report is a collaboration between the Office of the Minnesota Secretary of State and the School of Public Affairs Research Institute (SOPARI) of St. Cloud State University. All calculations and text are the result of work by SOPARI, which is solely responsible for errors and omissions herein.

Text authored by Professors King Banaian and Rich MacDonald of the Economics Department of St. Cloud State University. Research assistance provided by Nicholas Gross Kotschevar. Professor David Wall of the SCSU Geography Department provided GIS assistance.

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